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Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Special Access Rates for Price Cap Local Exchange Carriers	)	WC Docket No. 05-25
	)	
AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services	)	RM-10593

COMMENTS OF XO COMMUNICATIONS, LLC, COVAD COMMUNICATIONS GROUP, INC. AND NUVOX COMMUNICATIONS

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COVAD COMMUNICATIONS GROUP, INC. AND NUVOX COMMUNICATIONS

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XO Communications, LLC ("XO"), Covad Communications Group ("Covad"), and NuVox Communications ("NuVox") (collectively "Joint Commenters") hereby file these comments in response to the Commission's Public Notice asking parties to refresh the record in the above-captioned proceedings.[1]

I. INTRODUCTION AND SUMMARY

Rapidly approaching three years since initiating this proceeding to examine the regulatory framework and rates that apply to price cap local exchange carriers' ("LECs'") special access services and despite overwhelming evidence of market failure, the Commission has yet to take meaningful long-term action to address the Regional Bell Operating Companies' ("RBOCs") and other incumbent local exchange carriers' ("ILECs") detrimental exercise of market power in the markets for special access services. The competition that was predicted and used to justify deregulation has not

[1] *In the Matter of Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, *AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, RM-10593, Public Notice, FCC 07-123 (July 9, 2007).

materialized. In the absence of competitive or regulatory discipline, ILECs have used and continue to abuse their market power to command unjust and unreasonable rates for special access far in excess of those seen in competitive markets and to impose onerous and anti-competitive limitations in discount plans. Through the continuing use of exorbitant pricing and anti-competitive practices, RBOCs and other ILECs stifle competition and inflict harm on competitors and other consumers of special access services. All this, of course, has a significant detrimental impact on small businesses and consumer welfare. As some already have documented in this proceeding, the dead-weight costs to the national economy resulting from excessive special access pricing alone are staggering.

Since the 2005 filing of initial comments and replies in this proceeding, the evidence of market failure continues to mount with the gap between special access rates (either effectively or in real terms) and costs widening where Phase II pricing flexibility ("PRICE-FLEX") has been granted. As a result, the RBOCs' rates of return on special access services continue to ascend to supra-competitive levels, with two of them near or above a 100% rate of return. For 2006, rates of return for the RBOCs were 132.2% for Qwest, 99.6% for AT&T, and 57.4% for Verizon. Tellingly, the RBOCs continue to criticize these numbers as being "not right" without providing pricing comparisons or rate of return information they claim *is* right. Instead, the RBOCs' rely on inapt average revenue per unit figures, grossly distorted representations of the current state of facilities-based competition, and wildly inflated estimates of competition that may never materialize.

Meanwhile, current comparisons of special access prices to state commission approved cost-based rates for unbundled network elements ("UNEs") show special access rates significantly above those for corresponding UNEs. Price comparisons and analysis conducted by Joint Commenters in these comments provide compelling evidence that the market has failed to work as the Commission had hoped it would. Contrary to the expectation that competition would develop to drive special access rates to competitive levels, under the Commission's PRICE-FLEX regime, special access pricing has moved away from forward-looking costs rather than toward them.

Exacerbating this market failure is the fact that, since the initial comments and replies were filed, the RBOCs have absorbed through mergers the two largest (by far) competitive providers of special access. The only competitive providers with special access market shares that were at or near 10%, AT&T and MCI, are now part of the RBOCs. Further, the ability of remaining competitors to discipline ILEC pricing tactics for metro dedicated transport special access (channel mileage) is exceptionally limited, especially for DS1 circuits. The ability of competitors to discipline ILEC pricing tactics in the markets for various special access channel terminations is virtually nonexistent. Indeed, competitive local exchange carriers ("CLECs") are unable economically to self-supply or to obtain competitively provisioned alternatives to sub-OCn-level ILEC special access circuits.

Other recent regulatory developments have further increased the ILECs' market power in the provision of special access services. For instance, during the past two years, state commission implementation of the Commission's *Triennial Review ("TRO")* and *Triennial Review Remand Orders ("TRRO")* has resulted in significant limitations on CLECs' access to UNEs priced at forward-looking costs. Lacking virtually any competitive alternatives, competitors have had to convert nearly every high-capacity UNE loop (DS1 and above) lost to a non-impairment decision to unreasonably priced

ILEC-provided special access, much to the detriment of their customers and their businesses.

The manner in which Section 271 of the Act has been implemented in many states also serves to increase the market power of ILEC special access providers. In most states, ILECs have prevailed in largely equating Section 271 loop and transport checklist items with special access thus rendering Congress's enactment of the checklist a nullity. Only a few states have acted to give Section 271 teeth by ensuring that checklist items are priced at just and reasonable rates and then, the RBOCs immediately sought to reverse those decisions. Several of these states have been reversed in federal court and the others remain embroiled in litigation. One state, Georgia, requested guidance from the Commission on these matters. The Commission has not responded and its inaction continues to fuel the very regulatory uncertainty it repeatedly has acknowledged undermines the development of competitive markets. This inaction also fuels the growth of RBOC market power in the special access markets.

Notably, the market failure that has resulted in part from the Commission's decision to deregulate special access by granting pricing flexibility based on predicted competition rather than actual or effective competition recently was observed in a November 2006 study and report by the Government Accountability Office ("GAO").[2] In its report to the House Committee on Government Reform, the GAO determined that the Commission's pricing flexibility orders have resulted in increasing prices (in a declining cost industry) characterized by scant to non-existent competitive supply. The

2 *FCC Needs to Improve Its Ability to Monitor and Determine the Extent of Competition in Dedicated Access Services*, United States Government Accounting Office, Report to the Chairman, Committee on Government Reform, House of Representatives, GAO-07-80 (released Nov 2006) ("*GAO Report*").

GAO recommended that the Commission take action to better define effective competition and to consider additional data to measure competition. The Commission's unconvincing response to the report is that the costs of regulating special access are greater than those associated with the current PRICE-FLEX regime and that measuring actual competition somehow would be impractical or infeasible.

Today, all evidence points to the fact that the Commission must remedy its unrealized prediction of competition and premature deregulation of special access by eliminating Phase II pricing flexibility and by reinitializing special access rates. While re-initialization at forward-looking costs that approximate the pricing that would occur in a competitive market is one desirable solution, it may be more expedient, at least on an interim basis, to reinitialize special access pricing through the restoration of price caps based on an 11.25% rate of return. The Commission also should restore the X-factor, using 5.3% as the X-factor on an interim basis subject to further consideration. Immediate price relief is not the only relief that is essential to meaningful special access reform. The Commission also must act to proscribe exclusionary pricing practices and other anti-competitive terms and conditions in special access agreements, as such practices and terms deter facilities-based competition and diminish consumer welfare.

II. BACKGROUND

The Commission established price cap regulation of special access rates in 1991 to allow LECs to recover their costs and a reasonable profit while, at the same time, curbing the perverse incentives of more traditional rate-of-return regulation.[3] Rather than

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[3] *Policy and Rules Concerning Rates for Dominant Carriers*, CC Docket No. 87-313, Second Report and Order, 5 FCC Rcd 6786, 6818-20, ¶¶ 257-59 (1990)

limiting the profits a carrier might gain as rate-of-return regulation did, price cap regulation focused on the prices charged and resultant revenue earned from special access services, giving price cap LECs the incentive to reduce costs and increase efficiency in order to increase profits.[4] The initial price cap rates were set at levels existing when rate caps were imposed and then were adjusted annually based on a productivity factor (the "X-factor").

Additionally, two mechanisms allowed price cap LECs to establish rates above price cap levels. First, a low-end adjustment mechanism, whereby price cap indices were adjusted upward, was permitted if the LEC earned returns below a specified level in a given year.[5] Second, price cap LECs were allowed to set rates above the price cap levels if those rates would result in low earnings deemed to be confiscatory.[6] Thus, remedies were and continue to be available for an ILEC that believes its price cap regulated rates are too low. Furthermore, the Commission anticipated that competition would eventually eliminate the need for any rate regulation and "reserved the right to adjust rates in the future ***to bring them in line with forward-looking costs***."[7]

At the behest of the price cap LECs, the Commission adopted the *Pricing Flexibility Order* in 1999, where the Commission made predictions about the existence of

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("*LEC Price Cap Order*"), *aff'd Nat'l Rural Telecom Ass'n v. FCC*, 988 F.2d 174 (D.C. Cir. 1993).

4 Special Access Rates for Price Cap Local Exchange Carriers; AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services, *Order and Notice of Proposed Rulemaking*, WC Docket No. 05-25, ¶ 11 (Jan. 31, 2005) ("*Special Access NPRM*").

5 *Special Access NPRM* ¶ 12.

6 *Id.*

7 *Id.* ¶ 13 (emphasis added).

growing competition in certain metropolitan statistical areas ("MSAs") and allowed ILECs to offer special access services in those MSAs at unregulated rates via contract tariffs.[8] Specifically, the Commission predicted that the extent of collocation by competitors ("collocation trigger") would indicate the existence of irreversible competition which would discipline rates.[9] Under Phase I relief, a LEC may offer volume and term discounts and enter into contract tariffs, but it must continue to make generally available to all customers its regulated price cap tariff rates.[10] Under Phase II relief, a LEC is not required to conform to the regulated price cap rates.[11] According to

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8 *Access Charge Reform*, CC Docket Nos. 96-262, 94-1, 98-63, 98-157, Fifth Report and Order and Further Notice of Proposed Rulemaking, 14 FCC Rcd 14221, 14224-25, 14232-33, 14234-35, 14257-310, ¶¶ 77-83 (1999) ("*Pricing Flexibility Order*"), *aff'd WorldCom v. FCC*, 238 F.3d 449 (D.C. Cir. 2001).

9 *Special Access NPRM* ¶ 18; *Pricing Flexibility Order* ¶ 144. As demonstrated throughout these comments, the Commission's predictive judgment has proven to be in error. The Commission's decision also is flawed because it does not even permit the reversal of a pricing flexibility determination if the triggers are no longer met.

10 *Special Access NPRM* ¶ 17. To obtain Phase I pricing flexibility for interstate special access services other than channel terminations between a LEC end office and an end user's customer premises, a price cap LEC must demonstrate that unaffiliated competitors have collocated in at least 15% of the LEC's wire centers within an MSA or collocated in wire centers accounting for 30% of the LEC's revenues from these services within the MSA. To obtain Phase I pricing flexibility for channel terminations between a LEC end office and a customer premises, the LEC must demonstrate that unaffiliated competitors have collocated in at least 50 percent of the LEC's wire centers within an MSA or collocated in wire centers accounting for 65% of the LEC's revenues from these services within the MSA. 47 C.F.R. §§ 69.709, 69.711; *Pricing Flexibility Order*, 14 FCC Rcd at 14235-36, 14273-77, ¶¶ 24, 93-99.

11 *Special Access NPRM* ¶ 17. To obtain Phase II pricing flexibility for special access services other than channel terminations to end users, the trigger thresholds are unaffiliated collocation in 50% of the LEC's wire centers or in wire centers accounting for 65% of the LEC's revenues from these services within the MSA. For channel terminations to end users, the Phase II thresholds are unaffiliated collocation in 65% of the LEC's wire centers or in wire centers accounting for 85% of the LEC's revenues for these services. 47 C.F.R. §§ 69.709, 69.711; *Pricing Flexibility Order*, 14 FCC Rcd at 14235, 14298-300, ¶¶ 25, 146-52.

the GAO, "[s]ome level of pricing flexibility has since been granted to the four major price-cap incumbents in 215 of the 369 MSAs in the United States and Puerto Rico. These four price-cap incumbents have received full price deregulation (phase II for all circuit components) in 112 MSAs. Only 3 of the 100 largest MSAs [San Juan-Bayamon, Puerto Rico; Youngstown-Warren, Ohio; and Sarasota-Bradenton, Florida] in the United States and Puerto Rico are not under any pricing flexibility."[12]

In 2000, the Commission adopted the CALLS plan, which was intended to be a five-year interim regime to eliminate implicit subsidies in access charge rates and move toward a market-based approach to rate setting.[13] The Commission hoped that, by the end of 2005, sufficient competition would exist to discipline rates so that rate regulation would no longer be necessary. However, as the Commission recognized in the *Special Access NPRM,* such competition had in fact not developed by 2005 and thus the Commission decided to maintain the CALLS regime until conclusion of the instant proceeding.[14] Such competition still has not materialized.

The Commission, at the time, acknowledged that its regulatory regime might grant pricing flexibility before competition was substantial enough to actually discipline special access rates. It accepted that probability, however, because it deemed the costs of

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12 *GAO Report* at 6.

13 *Access Charge Reform*, CC Docket Nos. 96-262, 94-1, 99-249, 96-45, Sixth Report and Order in CC Docket Nos. 96-262 and 94-1, Report and Order in CC Docket No. 99-249, Eleventh Report and Order in CC Docket No. 96-45, 15 FCC Rcd 12962 (2000) (*CALLS Order*), *aff'd in part, rev'd in part, and remanded in part, Texas Office of Public Util. Counsel v. FCC*, 265 F.3d 313 (5th Cir. 2001), *cert. denied, Nat'l Ass'n of State Util. Consumer Advocates v. FCC*, 535 U.S. 986 (2002), *on remand, Access Charge Reform*, CC Docket Nos. 96-262, 94-1, 99-249, 96-45, Order on Remand, 18 FCC Rcd 14976 (2003).

14 *Special Access NPRM* ¶ 2.

continuing regulation higher than the risk of granting premature relief.[15] Believing that the ILECs could not exercise market power where they faced competition from entrants using their own facilities,[16] the Commission down-played evidence that the ILECs possessed high market shares for special access services despite the entrance of some competitive providers. Therefore, the Commission assumed that satisfaction of the collocation triggers it established would ensure adequate competition to prevent ILECs from charging unreasonable rates to customers with no competitive alternatives, from deterring market entry, or from engaging in exclusionary pricing behavior.

Almost before the ink was dry on the first orders granting Phase II pricing flexibility, ILECs began responding to that supposed price-constraining competition by raising their prices, not lowering them. As has been well documented in the record, the resulting harms to facilities-based competitors, small businesses, and consumers have been enormous.[17]

In late 2002, the legacy competitive provider AT&T filed a petition for rulemaking highlighting this market failure and requesting that the Commission essentially revoke its pricing flexibility rules and revisit the ILEC price cap rates established under the CALLS plan.[18] The Commission sought comment on that petition but did not act on it. In 2003, AT&T filed a petition for mandamus with the D.C. Circuit

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15 *Pricing Flexibility Order* ¶ 144.

16 *Pricing Flexibility Order* ¶¶ 69, 84-86.

17 *See, e.g.,* Ad Hoc Telecommunications Users Committee Comments, WC Docket No. 05-25, at 5 (June 13, 2005); Nextel Comments, WC Docket No. 05-25, at 9-12 (June 13, 2005).

18 *AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, RM-10593, Petition for Rulemaking at 6-7, 35-36 (filed Oct. 15, 2002) ("*AT&T Petition for Rulemaking*").

Court of Appeals, requesting the court to direct the Commission to take action. The mandamus petition effectively was mooted when the Commission adopted its *Special Access NPRM* in January 2005 to address the open issues raised in the *AT&T Petition for Rulemaking*.

Evidence presented by competitors in these proceedings demonstrates that the Commission was in error in granting Phase II pricing flexibility to the ILECs based upon predicted rather than actual competition. Furthermore, the findings released by the GAO in November 2006 are consistent with that evidence and clearly show that these non-competitive conditions and supra-competitive special access rates still exist today. Despite abundant evidence of market failure, the Commission has allowed far too much time to pass without correcting the competitive imbalance in the special access market.

On May 23, 2007, Rep. Edward J. Markey, Chairman of the House Subcommittee on Telecommunications and the Internet, expressed his concern that "significant concentration in the special access market through mergers and bankruptcies, combined with the Commission's deregulatory pricing regime, has resulted in higher prices and little competitive choice for special access connections."[19] Highlighting the GAO's findings, as well as the data in this record and in the recent merger proceedings, Chairman Markey urged the Commission to address these concerns by modifying its pricing flexibility rules so that special access rates will reflect those in a truly competitive marketplace.[20]

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19 Letter from Edward J. Markey, Chairman of the House Subcommittee on Telecommunications and the Internet, to the FCC, at 2 (dated May 23, 2007) ("*Markey Letter*").

20 *Id.* at 2.

In response to Chairman Markey's letter, the Commission issued a Public Notice requesting interested parties to refresh the record. Joint Commenters welcome the Commission's request to refresh the record in the instant proceeding. The Commission can no longer disregard the dearth of competition and the plight of captive carriers and consumers in special access markets. This Commission should insist that price constraining competition occurs before the deregulation of rates. Furthermore, because even the regulated price cap rates are excessively higher than cost, the Commission should reset price cap rates at a "just and reasonable" level, which can be done by reinitializing the price caps with an 11.25% rate of return and by reinstating the X factor at 5.3%.

III. EVIDENCE OF MARKET FAILURE IS UNDENIABLE

A company with market power is able, among other things, to impose substantial above-cost price increases over a sustained period without losing significant demand from its customers. The Commission itself has noted that "a substantial price increase need not be a large one;"[21] therefore, even a small increase in special access rates may indicate an abuse of market power. In this case, however, special access rates have increased dramatically since the Commission adopted its pricing flexibility rules. For example, T-Mobile reports that Qwest's special access rates increased 62% between 2002 and 2005 in areas that have been granted pricing flexibility, AT&T (legacy SBC) rates in PRICE-FLEX areas increased 27% between 2002 and 2005, and AT&T (legacy PacBell) rates in PRICE-FLEX areas increased 15% between 2002 and 2005.[22] As the greatly inflated returns indicate, the PRICE-FLEX regime has produced rates well in excess of

21 *Special Access NPRM* ¶ 74 & n.188.

22 Attachment 1, T-Mobile Presentation to NARUC at 6.

costs contrary to what is expected in competitive markets. And given that "[m]ore than half of the Bells' special access revenues come from areas where they are no longer subject to price cap regulation,"[23] this is no small concern. Because they lack competitive alternatives in most areas (despite supposedly having sufficient competition to justify pricing flexibility), special access customers competing with their ILEC suppliers must absorb these higher rates or stop serving their own retail customers. The RBOCs' special access customers must naturally pass on these rate increases to their own customers; therefore, "[b]y charging other carriers these inflated rates, the Bells also avoid retail price competition."[24]

A. Substantial and Sustained Above-Cost Rate Increases in MSAs Where ILECs Have Been Granted Phase II Pricing Flexibility and Soaring Rates of Return Provide Undeniable Evidence of Market Failure

As a direct result (and *prima facie* evidence) of rates far exceeding costs, the RBOCs' interstate special access rates of returns have skyrocketed in the years since pricing flexibility was permitted. AT&T's (based on combined legacy SBC and BellSouth data) rate of return increased from 40% in 2000 to 100% in 2006, Verizon's increased from 15% in 2000 to 52% in 2006, and Qwest's increased from 38% in 2000 to 132% in 2006.[25] The RBOCs have sought to counter these outrageous returns by nitpicking at the underlying, ARMIS-derived, data; however, there is no way to explain away the fact that these returns are well in excess of the Commission's initially prescribed rate of return of 11.25%. In fact, the Joint Commenters are unaware of any

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23 *AT&T Petition for Rulemaking* at 2-3.

24 *AT&T Petition for Rulemaking* at 4.

25 FCC Report 43-01, Table I Cost and Revenue, Column(s) Special Access, Row 1915 Net Return divided by Row 1910 Average Net Investment.

RBOC statement claiming their returns even approach this level. Simply put, claims of ARMIS data discrepancies and past under-earning cannot explain away or justify these outrageous rates of return.

The RBOCs also have argued that the increase in their special access revenues since gaining pricing flexibility in certain MSAs is due to growth in demand rather than increased and supra-competitive rates. To support their claims against reliance on the ARMIS-derived rates of return, the RBOCs try to convince the Commission that their special access revenue per line is the most relevant statistic to consider. They argue that the average revenue per line should be considered a proxy for special access rates and that the declining trend in their private calculation of those revenues indicates that special access rates also have been declining.[26] One must wonder why the RBOCs need to develop a proxy for special access prices when they have their actual pricing data at their fingertips. The reason why they hide behind a contrived annual revenue proxy is because their actual tariffed rates are so glaringly supra-competitive and the returns they produce are not those that could be expected in a competitive market.

As thoroughly discussed by Dr. Joseph Farrell, the former Chief Economist of the Commission, in his declaration already on the record, the RBOCs' assertion of the validity and significance of their special access revenue per line statistics is based on unsubstantiated data and erroneous assumptions.[27] Dr. Farrell explained that the RBOCs'

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26 *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, *Comments of Verizon, Declaration of William E. Taylor on Behalf of Verizon*, at 5, n.7 (filed June 13, 2005) ("*Taylor Decl.*").

27 *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, *Reply Comments of CompTel Global Crossing North America, Inc. and NuVox Communications, Reply Declaration of Joseph Farrell On Behalf of CompTel*, at 9-20 (filed July 29, 2005) ("*Farrell Decl.*").

conclusion that revenue per line has decreased cannot be verified because of the many assumptions and adjustments made by their economist, Dr. Taylor, in developing the revenue data.[28] Furthermore, Dr. Farrell explains that even without any price reduction, manipulation of the ARMIS access line count can show a decrease in revenue per line, based on how the number of utilized special access lines is captured in the ARMIS data.[29] Thus, average revenue per special access line does not reveal anything concrete about the RBOCs' special access prices. Furthermore, the competitor analyses of increases in actual RBOC tariffed rates from 2000-2005 belie the RBOCs' claims of reduced rates.

Finally, and critically, Dr. Farrell makes the fundamental point that even if the trend in RBOC special access rates was falling, this would not confirm a lack of market power because "[e]ven a monopoly will reduce price if marginal costs fall or if demand becomes more elastic."[30] He concludes by confirming that the relevant consideration for the Commission is not the rate of increasing (or even decreasing) rates, but rather the relative levels of price and cost,[31] underscoring the need for the comparison and analysis of RBOC special access rates and cost-based UNEs rates that Joint Commenters have undertaken below.

The Commission adopted Phase II pricing flexibility with the expectation that significant competitive forces would prevent an ILEC from exerting such market power. Industry data and experience have proven the opposite: that inadequate competitive forces have permitted ILECs to raise their prices to supra-competitive levels. As the

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28 *Farrell Decl.* at 10-11.

29 *Id.* at 11-13.

30 *Id.* at 16.

31 *Id.* at 16, 18.

GAO Report highlights[32] and as supported by competitor data analysis, the large price cap LECs consistently have increased their special access PRICE-FLEX rates well above costs. Notably, after a review of actual RBOC rates, not proxies, the GAO found that list prices and average revenues in Phase II MSAs tend to be higher than or the same as list prices and average revenues in areas still under some Commission price regulation.[33] Indeed, the GAO's analysis of 1,152 list prices and other data "generally shows that prices and average revenues are higher, on average, in phase II MSAs—where competition is theoretically more vigorous—than they are in phase I MSAs or in areas where prices are still constrained by the price cap." The GAO explained:[34]

> Since phase II pricing flexibility was first granted, list prices for dedicated access that apply under phase II, on average, have increased. Conversely, price-cap list prices available in phase I and price-cap areas were pushed downward over the same period—largely by the CALLS order. As a result, average list prices in areas with phase II flexibility are higher than average list prices in phase I and price-cap areas.[35]

Despite the existence of discount plans for customers that may enter into special contracts with the ILECs, as explained further below, the necessary volume and term commitments for carriers to obtain those discounts are often too onerous. Thus, while those discounts and lower rates may be available to some special access customers, they are not by any means universally available to all customers. Furthermore, while there may have been reasons, as the Commission has indicated, for ILECs to raise some price cap rates that

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32 *GAO Report* at 1.

33 *Id.*.

34 *Id.* at 13.

35 *Id.* at 13.

may have been below cost, there can be no valid justification for the consistently higher rates found in Phase II MSAs than in Phase I MSAs.

A recent Progress & Freedom Foundation ("PFF") Report on special access attempts to undermine the GAO findings by asserting, although without "definitive conclusions," that pricing flexibility itself may have led to increased ILEC investment (using quantity of lines sold as a proxy for investment),[36] suggesting that the increase in ILEC output indicates no abuse of market power. This study, as its author admits, "is incomplete because it has ***no information on prices.***"[37] Its results are thus fundamentally suspect.

B. Comparisons of Special Access Prices to Forward Looking Cost-Based UNE Rates for Comparable Services Provide Compelling Evidence That, with Few Exceptions, Special Access Rates in Most Instances Are Not Just and Reasonable

The Commission has stated its preference for special access rates to move toward a cost-based rates. In the *Access Charge Reform Order* the Commission put the ILECs on notice that "[t]o the extent that competition did not fully achieve the goal of moving access rates toward costs, the Commission reserved the right to adjust rates in the future to bring them into line with forward-looking costs."[38] The best estimates of the ILECs' forward-looking costs of providing special access services are naturally the cost-based UNE rates for comparable services.[39] To provide updated pricing information for the Commission, Joint Commenters have compiled and analyzed a sampling of RBOC rates,

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36 Scott Wallsten, *Has Deregulation Affected Investment in Special Access?*, at 10 (released by the Progress & Freedom, July 2007) ("*PFF Report*").

37 *Id.* at 11 (emphasis added).

38 *Access Charge Reform* CC Docket No. 91-212, First Report & Order, 12 FCC Rcd at 15982, 16002-03, ¶ 47.

39 *See Farrell Decl.* at 18-20.

which demonstrate that the rates for special access channel terminations and mileage are, with rare exception, significantly higher than for comparable TELRIC-based UNE rates. These comparisons ultimately indicate that special access rates are excessively above cost and are therefore unjust and unreasonable.

Joint Commenters selected several states served by each RBOC and focused analysis on the highest density zone in each of those states, where costs should be the lowest in the state and the level of competition (at least theoretically) the highest.[40] These comparisons show that special access rates are substantially above forward-looking costs (with few exceptions). This disparity in pricing, especially in these high density study areas, constitutes anti-competitive behavior and the abuse of market power.

In all the states analyzed, the month-to-month recurring price cap recurring rates (no term commitment) for DS1 loops/channel terminations are vastly higher than the UNE DS1 loop rates, ranging from 67% higher in Arizona to 802% higher in Illinois.[41] The month-to-month recurring Phase II pricing flexibility rates are all at least 100% higher than the UNE DS1 loop rates, with many of the state Phase II rates 200-300% higher than the cost-based UNE rates.[42] Significantly, in all but one state surveyed, the Phase II pricing flexibility rates were also higher than the regulated price cap rates in the highest density zone in the state.[43]

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40 *See* Attachment 2. Joint Commenters compared and analyzed RBOC special access and UNE pricing data from the following states: Arizona, California, Colorado, Georgia, Illinois, New York, Pennsylvania, Texas, and Virginia.

41 Attachment 2, *Comparison Of UNE DS1 Loop And Special Access Rates*, *For Qwest in Arizona & For AT&T in Illinois*.

42 Attachment 2, *Comparison Of UNE DS1 Loop And Special Access Rates* (for all states).

43 Attachment 2 , *Comparison Of UNE DS1 Loop And Special Access Rates (for all states)*. In accordance with the conditions of its merger with BellSouth, AT&T

In a competitive environment, one would expect that special access rates would tend to be closer to cost-based rates as customers are required to commit to longer terms of service. The data, however, does not bear that expectation out. Where the surveyed carriers offer a 1-year term commitment special access contract, both the price cap rates and the Phase II rates for DS1 channel terminations are still considerably higher than the UNE DS1 loop rates, with the price cap rates ranging from 62% higher in Arizona to 585% higher in Illinois and the Price-Flex II rates ranging from 131-607% higher.

Even 3-year special access term plans do not significantly reduce the disparity between the UNE loop rates and either the price cap rates or Phase II rates for ILEC special access channel terminations. Under available 3-year plans, price cap rates are still 52-268% higher and Phase II rates are 75-272% higher than the cost-based UNE rates.[44]

The non-recurring charges ("NRCs") for special access channel terminations also are exorbitantly higher than those charges for UNE DS1 loops, with charges in Texas, Pennsylvania, and Virginia all being over 1,000% higher than the non-recurring charge permitted for UNE services.[45] Verizon does not offer a 1-year term commitment plan and its special access NRCs in Pennsylvania and Virginia are reduced under its 3-year term commitment; however, AT&T's $900 special access NRC (applied under both price caps and Price-Flex) in Texas, as compared to the $76 UNE NRC, continues to apply for its 1-year term commitment but is waived if a customer commits to a 3-year term.

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recently reduced its Price-Flex rates to the level of its price caps in Georgia, as well as in other merger-related states not surveyed.

44 Attachment 2 , *Comparison Of UNE DS1 Loop And Special Access* Rates (for all states).

45 Attachment 2, *Comparison Of UNE DS1 Loop And Special Access Rates, For AT&T in Texas, For Verizon in Virginia, & For Verizon in Pennsylvania.*

Qwest's special access NRCs in Arizona and Colorado are 75-85% higher than the UNE NRCs and apply even when a customer commits to a 3-year term.[46]

Rate comparisons for DS1 dedicated transport UNEs and special access channel mileage show similar, if not more extreme, disparities between UNE rates and both price caps and Phase II pricing flexibility rates for special access. At the outset, special access rates for channel mileage and UNE rates for DS1 transport include at least two rate elements: the fixed monthly rate and the mileage rate which varies according to the length of the circuit. The fixed month-to-month recurring Phase II rates for most of the areas analyzed are over 100% percent higher than for the comparable UNE services, with both price cap rates and Phase II rates over 400% higher than the UNE rates in Illinois.[47] The greatest disparity is in mileage rates, where the special access rates in some instances over 10,000% higher than the comparable UNE rate in the state. For example, in Texas the UNE fixed monthly and mileage rates are $33.76 and $0.1005, respectively; the price cap fixed monthly and mileage rates are $62.00 and $15.50; and the Phase II fixed monthly and mileage rates are $85.00 and $18.00.[48] Importantly, in Texas and all but two other states in the study, the Phase II rates exceed the regulated price cap rates by 15-40%.[49]

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46 Attachment 2 , *Comparison Of UNE DS1 Loop And Special Access Rates, For Qwest in Arizona & For Qwest in Colorado.*

47 Attachment 2, *Comparison Of UNE DS1 Transport And Special Access Rates, For AT&T in Illinois.*

48 Attachment 2, *Comparison Of UNE DS1 Transport And Special Access Rates For AT&T in Texas.*

49 Attachment 2, *Comparison Of UNE DS1 Transport And Special Access Rates,* (for all states). In accordance with the conditions of its merger with BellSouth, AT&T recently reduced its Price-Flex rates to the level of its price caps in Georgia, as well as in other merger-related states not surveyed.

Similar to the loop data, one would expect that, even if the month-to-month transport rates remained somewhat higher, there would be a dramatic reduction in rates when customers commit to longer terms. As with the loop rates, however, even the longer-term transport rates remain supra-competitive and well above the cost-based UNE rates. For RBOCs that offer a 1-year term discount – Verizon does not – the price cap and Phase II fixed rates for transport are 43-292% and 79-350% higher than UNE rates, respectively.[50] The rates for a 3-year term are not dramatically better and are still over 100% percent higher than UNE rates in some states.[51] In several Verizon states, for example, where the fixed recurring monthly rates for its month-to-month and 3-year plan are actually lower than the comparable UNE fixed rate, the excessive mileage charges that are 371-4,462% above cost allow Verizon to recover its costs and still effectively undermine its competitor customers.[52] Here, too, the most glaring differences in rates are for mileage for both 1-year and 3-year terms, which, even with the term commitment, are over 1,000% higher than the comparable UNE rates for many states.[53]

C. Neither Merger Conditions Nor Court Decisions Cure the Evident Market Failure

In 2005, the Commission approved the SBC/AT&T and Verizon/MCI mergers subject to conditions including reducing and freezing special access rates for 30

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50 Attachment 2, *Comparison Of UNE DS1 Transport And Special Access Rates,* (for all states).

51 Attachment 2, *Comparison Of UNE DS1 Transport And Special Access Rates, For Verizon in New York; For Verizon in Pennsylvania; & For Verizon in Virginia.*

52 Attachment 2, *Comparison Of UNE DS1 Transport And Special Access Rates,* (for all states).

53 Attachment 2, *Comparison Of UNE DS1 Transport And Special Access Rates,* (for all states).

months.[54] Additional conditions were imposed as part of the 2006 merger of AT&T with BellSouth. These conditions, while marginally helpful, are not truly beneficial for consumers and competitors. First, these conditions are limited in time. Second, they address competitive harms arising from the mergers and not the basic problem of market power in the special access markets. Rates that were already unjust and unreasonable, which they were, would continue to be unjust and unreasonable. Finally, the conditions are carrier-specific and do not apply to other ILECs.

The collocation triggers devised by the Commission as a basis for special access price deregulation have not proven to be accurate predictors of the advent of price constraining competition. The Commission dismissively justified its decision to adopt collocation triggers by citing to the D.C. Circuit Court of Appeals' affirmation of its rationale in its *Pricing Flexibility Order*.[55] But the fact that the court found the adoption of collocation triggers to be a reasonable approach does not mean that it was the right approach or that retaining it remains justifiable. "[A]s the courts have stressed, where, as here, the Commission has based its existing regulatory regime on a predictive judgment, it is absolutely imperative that "the Commission . . . vigilantly monitor the consequences of its rate regulation rules."[56] Rather than blithely ignoring the impact of its pricing flexibility regime, the Commission must review the clear data and analyses presented in

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54 *SBC Communications Inc. and AT&T Corporation Applications for Approval of Transfer of Control*, Memorandum Opinion and Order, WC Docket No. 05-65 (rel. Nov. 17, 2005); *Verizon Communications Inc. and MCI, Inc. Applications for Approval of Transfer of Control*, Memorandum Opinion and Order, WC Docket No. 05-75 (rel. Nov. 17, 2005).

55 Letter from Kevin J. Martin, Chairman of Federal Communications Commission, to The Honorable Joseph I. Lieberman, Chairman, Committee on Homeland Security and Governmental Affairs, at 2 (Jan. 29, 2007).

56 AT&T Petition for Rulemaking at 6 (citing American Civil Liberties Union v. FCC, 823 F.2d 1554, 1565 (D.C. Cir. 1987)).

this proceeding to assess the tenuous state of competition in the special access market. Because competitive forces are inadequate to constrain the ILECs' monopoly behavior, the Commission should rescind Phase II pricing flexibility and impose reasonable regulated rates.

D. Despite Above-Cost Rates in MSAs Where ILECs Have Been Granted Phase II Pricing Flexibility, Widespread Competitive Entry Has Not Occurred and Few Competitive Alternatives Exist to Discipline Special Access Rates to a Competitive Level.

A key reason that the ILECs are able to sustain supra-competitive rates for special access is because of the lack of facilities-based competitive alternatives. As explained in the attached Declaration of Ajay Govil, XO's Director of Transport Technology and Network Architecture, there are multiple reasons for this scarcity. First, it remains inefficient for most CLECs to build high-capacity loop facilities themselves.[57] Second, interconnecting with the few competitive access providers ("CAPs") that do exist provides little in the way of economic benefit.[58] Finally, no other technology has yet developed as a widely available wireline loop substitute.[59]

Except in rare instances, it is uneconomic for CLECs to build their own high-capacity facilities to their customers. For a CLEC to provide its own facilities, the demand must be so great that it overcomes the large, sunk cost incurred in provisioning service directly to the customer. **BEGIN CONFIDENTIAL**

57 XO *Govil Decl.*, ¶ 12-21.

58 *Id.*, ¶ 29.

59 *Id.*, ¶ *25*

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CONFIDENTIAL To justify this level of expense, a CLEC must have the equivalent of at least three DS-3s worth of capacity under contract from the occupants of such a building.[61] Any less and the CLEC must find another way to provision service or risk taking a major loss on its investment.

Only the very largest customers need three DS-3s worth of capacity. Most customers, including most small- and medium-sized businesses, will function perfectly well with DS-1 level access or metro Ethernet-level access which increasingly fills the gap between DS1 and DS3 TDM-based services. The Commission's *TRO* finding that CLECs "face extremely high economic and operational barriers" in deploying DS1 loops remains true today.[62] The Commission also recognized that small- and medium-sized business customers who use DS-1 level access present significantly different characteristics from large enterprise customers, and that such smaller customers are generally resistant to the type of long-term contract that would justify building out facilities to the customer's location.[63]

The lack of competitive access providers offering economical services also directly increases CLEC reliance on ILEC special access.[64] For the reasons discussed above, very few competitive access providers can offer on-net ("Type I") end-to-end service. On the rare occasion when Type I services are offered, such services are

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60 *Id.*, ¶ 17.

61 *Id.* ¶ 10, 20.

62 TRO ¶ 325.

63 *Id.*

64 XO *Govil Decl.* ¶ 28.

generally priced significantly less than ILEC special access and can be a very attractive option for CLECs.[65]

Unfortunately, the vast majority of competitive access providers must make use of ILEC special access services or ILEC UNEs themselves to provide wholesale service reaching to the end user's location ("Type II" services). CLECs generally do not favor purchasing Type II facilities because the underlying provider does not control the entire facility. In addition, while purchasing Type II services from a competitive access provider may provide some cost savings, such savings are generally not significant because Type II service providers must pass on the price they paid to the ILEC for special access plus its own markup.[66] Finally, as a result of the *TRRO*, many UNEs have been eliminated and converted to significantly higher, non-cost-based priced special access. This has caused prices to rise for all CAPs, including those providing Type II services. As a result, many Type II services are now generally equivalent to, if not above, the price for ILEC special access.

For these reasons, CLECs like Covad, NuVox, and XO make very little use of CAP provided loops. Currently, less than **BEGIN CONFIDENTIAL END CONFIDENTIAL** of Covad's and NuVox's loop access needs are met by using competitive alternatives to ILEC special access.[67] XO also currently uses alternative loop access providers for only a small part of its needs.[68]

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65 XO *Govil Decl.* ¶ 28; NuVox *Coker Decl.* ¶ 5.

66 *Clancy Decl.* ¶ 6.

67 Covad *Clancy Decl.* ¶ 7; NuVox *Coker Decl.* ¶ 5.

68 XO *Govil Decl.* ¶ 28-29.

The failure of intermodal platforms to develop into widely available substitutes for ILEC special access, even with special access priced so far above cost, has also helped the ILECs maintain their stranglehold on last-mile service.[69] Although fixed wireless services are starting to be deployed successfully, there is nothing close to ubiquitous coverage and obstacles, presented by the ILECs, have limited deployment. For the past year, XO has been seeking to obtain collocation for microwave facilities at buildings owned by AT&T where XO and others are collocated; yet, AT&T has thwarted XO at every turn, such that, over one year since it began seeking to collocate its facilities, none have been deployed.

Cable television systems also have not developed in a manner that allows them to serve as alternatives for widespread deployment of DS-1 or DS-3 loop facilities. Most cable televisions systems were designed to serve residential customers in suburban areas. Thus, commonly the cable television systems do not reach the customers to whom the CLECs need to connect.[70] Where cable television networks reach business customers, they generally lack the capacity to serve large numbers of business customers that require telecommunications and Internet services at DS1 and higher speeds. While some cable networks have been developed to provide high bursts of speeds to smaller customers, few cable systems are capable of meeting the high bandwidth requirements of larger customers like those serviced by XO, Covad and NuVox.[71]

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69 Because customers for special access services demand reliability, high quality, and high speed, many of the frequently mentioned alternatives, such as satellite, broadband powerline, or mobile wireless services, are very poor substitutes.

70 XO *Govil* ¶ 22-24.

71 XO *Govil* ¶ 24.

E. The Terms and Conditions of ILEC Price-Flexibility Tariffs and Contracts Are Onerous and Exclusionary

The Commission also has recognized that market power can be exercised through exclusionary conduct as evidenced by onerous terms and conditions in a LEC's tariff offerings.[72] Because special access services are characterized by economies of scale and significant sunk costs, with impediments such as rights-of-way and building access, market entry by competitive providers has been limited and generally concentrated in the highest capacity services in the densest metropolitan areas.[73] Additional barriers to entry other than these economic and operational impediments may be imposed unreasonably by the ILECs to prevent competition in both the wholesale and retail markets for these services. As the Commission's former chief economist explained:

> Among such incremental impediments to entry would be (a) excessive charges (typically payable by the customer) for terminating ILEC service, (b) commitments to purchase some minimum amount from the incumbent, with substantial penalties for non-compliance, and (c) any provisions such as volume or loyalty discounts under which a special access consumer pays the ILEC more for something else (such as service at another location) if it uses an entrant rather than ILEC special access in one location.[74]

Although such contracts may not have exclusionary effects in a competitive environment, exclusionary or anti-competitive conduct often arises when an incumbent with market power is the only entity that can supply each customer's entire demand.[75] As discussed

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72 *Special Access NPRM* ¶ 114.

73 *Farrell Decl.* at 2.

74 *Farrell Decl.* at 2.

75 *AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, RM-10593, *Reply Comments of WorldCom, Inc., Declaration of Michael D. Pelcovits On Behalf of WorldCom Inc*, at 8 n.6 (filed January 23, 2003) ("*Farrell Decl.*").

above, the ILECs have the market power to succeed with anti-competitive behavior and have strong incentives to use exclusionary pricing to prevent entry and expansion of the competitors.[76] As explained in declarations already on the record, especially by Drs. Pelcovits and Farrell, such practices were widespread years ago when the Commission initiated this proceeding. These practices continue to plague competitors in the industry today.

To avoid paying the most excessive of the special access rates discussed above (*i.e.,* the month-to-month rates), special access customers have little choice but to enter into contractual arrangements with the ILECs where they obtain discounts off month-to-month special access rates in exchange for committing to unreasonable purchase volumes or term periods. The RBOCs claim that most of their customers purchase from contracts providing significant discounts off of their month-to-month special access rates. Many of those contracts, however, contain onerous conditions that few customers are able to meet or that lock-in customers unreasonably foreclosing other supply options. For example, Verizon recently offered a National Discount Plan ("NDP") created for and targeted primarily to a single very large carrier with volume commitments much higher than any CLEC could achieve to gain the discounts.[77] Additionally, many of the volume discounts include growth components requiring carriers to increase their volume commitments annually. Often, the required growth rates are higher than a carrier's historical trend. This indicates that the required growth rates are too high for that competitor to realistically achieve without incurring penalties. Thus, many competitors are left with

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76 *Farrell Decl.* at 9.

77 The Verizon Telephone Companies, TARIFF F.C.C. No. 1, Original Pages 25-40 Section 25.3 (effective June 9, 2007).

little choice other than to purchase from the highest base month-to-month special access rates.

Additionally, AT&T's special access tariff offerings and discount plans are administered at the regional level based on AT&T's legacy companies (Pacific Telesis Group, Ameritech, Southwestern Bell, BellSouth, and SNET) and do not allow volume commitments to be met with services throughout the entire consolidated AT&T region. AT&T also does not easily allow portability, or the substitution of one circuit for another to meet volume commitments, throughout all of its legacy sub-regions, so competitors may be subject to early termination penalties in some areas if a circuit is disconnected before the end of the committed term.[78] Because these terms are managed at the legacy regional level rather than throughout the incumbent's entire service territory, competitors cannot combine their purchases throughout the region to satisfy the cumbersome minimum requirements. Unlike AT&T, who can offer a retail customer a comprehensive rate plan that would span its vast nationwide service territory, a competitor's ability to manage its own large national customers is more limited because it must adjust and account for various differing rate plans and requirements.

Moreover, while the RBOCs argue that term commitments ensure they are able to recoup their necessary costs, term commitments with onerous termination penalties when imposed by firms with market power have anti-competitive effects. For example, Verizon's Commitment Discount Plan ("CDP") requires a minimum two-year term to qualify for discounts. Additionally, Qwest's month-to-month special access rates are so excessive that carriers are induced to commit to a one-year term to gain more reasonable rates. The termination penalties for most of these ILEC discount plans are unreasonable

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78 Covad *Clancy Decl.* ¶ 13; XO *Govil Decl.* ¶ 34.

because the customer must pay some of the remaining months at the full monthly rate even if the circuit is disconnected well before the end of the first year. For example, under Qwest's Regional Commitment Plan ("RCP"), if a customer terminates service within the first 12 months of any of its term plans, the customer will incur an early termination penalty of 100% of its contracted monthly charges for the remaining months of the first year.[79] The customer would additionally pay 50% of its committed monthly charges for the remaining months of the contract.[80] A customer is also subject to a shortfall if its actual volume of circuits falls below its committed monthly volume. In this case, the customer is charged a shortfall based on the average circuit price multiplied by the difference between its actual circuits in service and its committed volume.[81] Therefore, for example, a competitor utilizing an ILEC's special access services to provide retail services to its customer must require that customer to commit to a minimum term or risk being subject to an extreme termination penalty. This leaves competitors at a significant disadvantage in the retail market because Verizon need not require its own retail customers to commit to a two-year minimum term.

The RBOCs have justified their excessive termination penalties as a way of preventing customers from obtaining discounts in the short term and then canceling service when they no longer meet the volume requirements.[82] A termination penalty

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79 Attachment 3, Qwest Communications, TARIFF F.C.C. NO. 1, 3rd Revised Page 7-154, Section 7.1.8(B) (Effective December 16, 2003).

80 Attachment 3, Qwest Communications, TARIFF F.C.C. NO. 1, 2nd Revised Page 7-106, Section 7.1.3(B)(5) (Effective February 1, 2006).

81 Attachment 3, Qwest Communications, TARIFF F.C.C. NO. 1, 3rd Revised Page 7-104, Section 7.1.3(B)(3)(c) (Effective February 1, 2006).

82 *Opposition of Qwest Communications , Declaration of Alfred E. Kahn and William E. Taylor On Behalf of BellSouth Corporation, Qwest Corporation, SBC Communications, Inc., and Verizon*, at 32 (filed December 2, 2002) ("Kahn & Taylor Declaration").

imposed by a firm with market power which requires payment of the full amount (or a large percentage) of the contract through the entire term of the contract even after it has terminated service, however, is punitive in nature, and is not based on cost recovery. Since even the discounted special access rates greatly exceed cost-based rates for comparable UNEs, such a penalty implies the RBOCs have more nefarious purposes: to drive up the wholesale costs of its competitors and to lock-in its customers so they are unable purchase circuits from a competitor.[83] Because of the short supply of competitive alternatives for special access circuits, neither wholesale nor retail customers have the option of selecting another provider of special access that may not impose such termination penalties; therefore, the RBOCs are able to use their market power to impose these onerous conditions on their customers, which also operate to exclude their competitors from the market.

Even without the excessive volume and term commitments, ILEC special access contracts contain anti-competitive provisions. For example, several AT&T contracts require that at least 4% of services ordered must be switched over from a non-incumbent provider.[84] This anti-competitive requirement is included solely to draw business away from AT&T's competitors and must be prohibited. By tying up customers and requiring business to be moved from its competitors, AT&T is able to further strengthen its significant power in the market.

Additionally, AT&T has adopted pricing plans that undermine a competitor's ability to offer discounts to customers for a particular service because the competitor

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83 *See Pelcovits Decl.* at 5; *Farrell Decl.* at 2.

84 *GAO Report* at 31, Table 4 (*citing*, Southwestern Bell Contract No. 15, Ameritech & Pacific Bell Contract No. 20, and Southern New England Telephone Contract No. 1.

would lose discounts it had obtained from AT&T on other services.[85] For example, in order to obtain discounts under AT&T's Managed Value Plan for both for its legacy Ameritech and Southwestern Bell regions ("MVP"), competitors must not only commit to minimum annual revenue requirements ("MARCs") of $10 million in each region, but they must also maintain an Access Service Ratio of 95% or greater, meaning that no more than 5% of a competitor's monthly billing with AT&T may be for UNEs, including DS1 and DS3 UNE loops, and DS1, DS3 and dark fiber UNE transport.[86]

Volume and growth requirements, coupled with termination penalties, of AT&T's MVP impede a competitor's ability to win or retain a customer who may already be on this plan with AT&T. The retail customer receives a discount only on amounts up to the MARC but not over the MARC, creating an incentive for customers to increase the MARC as its needs grow in order to receive the discount on its growth rather than paying the base special access rates. Although the MARC may be increased, it may not be decreased during the term of the plan. Because the MARC is based on 100% of historical revenues and because it cannot be decreased, a customer whose demand does not grow cannot switch to a competitive carrier for part or all of its special access spending without incurring significant penalties.[87] Customers who fail to meet the MARC either incur a shortfall penalty or an excessive termination penalty, including repayment of the past six

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85 *Pelcovits Decl.* at 15.

86 Ameritech Operating Companies,TARIFF F.C.C. NO. 2, 3rd Revised Page 663 & 5th Revised page 664, Section 19.3(D) (Effective June 8, 2002), Southwestern Bell Telephone Company TARIFF F.C.C. NO. 73, 3rd Revised Page 38-6 & 3rd Revised Page 38-7, Section 38.3(D) (Effective June 8, 2002).

87 *Farrell Decl.* at 5-6.

months' discounts, if the contract is cancelled.[88] AT&T's MVP tariff fits the pattern of an exclusionary contract by tying the offered discounts to maintaining traffic on AT&T's network, and creates a very large hurdle for competitors to overcome.[89] "These provisions, and others like them in the various term and volume discount plans offered by the ILECs, artificially increase a customer's cost of switching, and raise competitors' costs of acquiring customers.

Verizon also has offered a promotion in connection with its UNE forbearance petitions that required competitors' high-capacity UNEs to be converted to special access in order to qualify for lower special access pricing.[90] For companies that rely extensively on UNEs, some of which have a current ratio of special access to UNEs of less than 10%, this requirement is obviously unreasonable because there is no way for these carriers to take advantage of special access discounts without converting most of their circuits from UNEs to higher priced special access. This requirement is anti-competitive because it requires competitors to forego their rights to purchase UNEs at lower cost-based rates and instead to rely almost entirely on higher-priced and virtually unregulated special access. Moreover, there is no cost justification for this requirement. The only reason for it is to drive up the ILEC's competitors' costs.

Extensive long-term commitments and growth requirements imposed by a firm with market power discourage and prevent competitors from seeking out competitive alternatives or self-provisioning once they are locked into an ILEC special access term

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88 Ameritech Operating Companies, TARIFF F.C.C. NO. 2, 3rd Revised Page 677 & 2nd Revised Page 678, Section 19.3(J)(Effective April 10, 2002); Southwestern Bell Telephone Company TARIFF F.C.C. NO. 73, 2nd Revised Page 38-21 & 2nd Revised Page 38-21.1. *See also*, *Farrell Decl.* at 3-4; *Pelcovits Decl.* at 14.

89 *Pelcovits Decl.* at 14-15.

90 Covad *Clancy Decl.* ¶ 12.

commitment.[91] After committing to 3-year or 5-year terms, competitors are prevented during that time from converting their high-priced ILEC special access services to lower-cost alternatives from other vendors or via self provisioning without incurring significant termination penalties. By targeting the growth market where competition or entry would be most likely, the ILECs can prevent the development of a more facilities-based competition.[92]

Even a one-year term commitment in the hands of the RBOCs may be anti-competitive. In a situation where no UNE facilities are readily available, a competitor may provide service temporarily via special access services with the intention of converting that customer to UNE-provided services shortly after provisioning. The competitor must continue purchasing special access circuits even though a lower-priced UNE alternative has become available. With even a one-year minimum term for special access services, the ILEC is able to intentionally lock its competitors into utilizing special access longer than they would otherwise do so, significantly and artificially increasing the competitors' costs.

Joint Commenters certainly do not wish to undermine the ILECs' ability to offer discounts off of their base special access rates. ILEC special access discounts, however, should come without such anti-competitive strings attached since customers have no alternatives for a large share of their business.[93] Exclusionary pricing, in contrast to predatory pricing, can be virtually costless because it does not require the offending entity to ever set price below its own costs, thereby eliminating the need to later recoup

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91 *Pelcovits Decl.* at 13.

92 *Id.*

93 *Id.* at 16.

those costs.[94] By inducing enough buyers to sign long-term, high volume or growth contracts, the ILEC can tie up enough customers and volume such that there is insufficient demand available for competitors to enter the market and operate profitably.[95]

More generally, the ILECs also continue to attempt to constrain competitors' abilities and rights to challenge the excessive special access rates and charges imposed upon them. When additional charges, such as those for special construction, are required they are often are not adequately explained or detailed. Some ILEC discount plans restrict a competitor's ability to dispute charges or prevent any disputed charges to count toward minimum commitments even if the competitor later pays the charges.[96] Other plans attempt to restrict competitors' rights to seek regulatory recourse by forbidding them from participating in regulatory proceedings that condemn the ILEC's excessive special access rates.

In the special access market, both supply responsiveness and demand responsiveness are low, allowing the LECs to hold onto market power and exercise it at will. Supply responsiveness measures whether competitors enter the market with enough capacity to supply competing services when a LEC increases rates for special access. Demand responsiveness measures whether consumers have the ability to make a switch to a competitor if such an alternative exists. As discussed above, there are very few special access competitors remaining in the market, and none that have the capacity to satisfy demand throughout the market. Furthermore, the exclusionary pricing plans employed by the LECs lock-in customers so they are often unable to switch to an

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94 *Id.* at 5-6.

95 *Id.* at 5-9.

96 XO *Koppersmith Decl.* ¶ 6.

alternative carrier, even if one exists. Thus, because drastically above-cost ILEC rates have not induced competitive entry and the largest competitors in the market have exited due to mergers with the ILECs, there is not nearly enough competition to discipline the rates, terms and conditions of ILEC special access services.

IV. RECENT REGULATORY DEVELOPMENTS DRIVE DEMAND FOR INCUMBENT LEC SPECIAL ACCESS, IRRESPECTIVE OF COSTS

Since the initial filing of comments and reply comments in this proceeding, changes within the industry have stalled competition within the market for special access services, and at the same time, have eliminated loop and dedicated transport facilities and services that CLECs tend to use as special access service substitutes. In only two years, the industry witnessed the simultaneous mergers of dominant special access service providers, Verizon and SBC, each with their biggest in-region competitor, MCI and AT&T. Subsequently, the new "AT&T" swallowed BellSouth, thereby narrowing competition within the market for special access services within nine additional states. Importantly, as the selection of special access service providers has become smaller, so has the selection of substitute services. In particular, the Commission's most recent rule changes, limiting the high-capacity loop and dedicated transport UNEs available to competitors, have only increased the ILEC's market power for special access services.

A. Recent Mergers Have Eliminated the Two Largest Competitive Providers of Special Access Services

Since the initial filing of comments in this proceeding, the Commission has approved three RBOC mergers, resulting in substantial, industry-wide impact. In November 2005, the Commission approved the mergers of Verizon and MCI, and of SBC and AT&T.[97] In December 2006, the Commission approved the acquisition of BellSouth by the "new" (*i.e.*, post SBC-merger) AT&T.[98] As the result of these mergers, the telecommunications industry is, and special access markets are now, dominated by two giants, each of which provide service within more than 20 states.[99]

Among other things, those mergers reduced both actual and potential competition among providers of special access services within each of the former operating territories of BellSouth, SBC, and Verizon, leaving customers to rely primarily on the special access services offered by the two RBOCs.[100] Because little or no competition exists within the markets for various special access services, the ILECs now, more than ever, have broad discretion to increase rates for special access services far above cost, and to condition discount service arrangements on terms that harm customers and discriminate against

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97 *SBC Communications Inc. and AT&T Corp. Applications for Approval of Transfer of Control*, WC Docket No. 05-65, Memorandum Opinion and Order, FCC 05-183 (rel. Nov. 17, 2005) ("SBC/AT&T Merger Order"); *Verizon Communications Inc. and MCI, Inc. Applications for Approval of Transfer of Control*, WC Docket No. 05-75, Memorandum Opinion and Order, FCC 05-184 (rel. Nov. 17, 2005) ("Verizon/MCI Merger Order").

98 *In the Matter of AT&T Inc. and BellSouth Corporation Application for Transfer of Control*, Memorandum Opinion and Order, 22 FCC Rcd 5662 (2007) ("AT&T/BellSouth Merger Order").

99 The Form 10-K of Verizon Communications Inc. (Part I, Item I) filed with the United States Securities and Exchange Commission on March 7, 2007 reflects that Verizon provides wireline telephone services to customers within 28 states, and the District of Columbia. The Form 10-K of AT&T Inc. (Part I, Item I) filed with the United States Securities and Exchange Commission on February 26, 2007 reflects that AT&T's "traditional wireline subsidiaries " provided long distance and local telephone services within 13 states, as of December 31, 2006. After acquiring BellSouth's operating subsidiaries, on January 1, 2007, AT&T provides wireline telephone services within 21 states.

100 Comments of Cbeyond *et al.*, WC Docket No. 06-74, at 63-74 (filed Jun. 5, 2006); Petition to Deny of CompTel, WC Docket No. 06-74, at 7-8 (filed Jun. 5, 2006); Comments of Sprint Nextel Corporation, WC Docket No. 06-74, at 11-12 (filed Jun. 5, 2006); Petition to Deny of Time Warner Telecom, WC Docket No. 06-74, at 16-25 (filed Jun. 5, 2006).

competing providers.[101] The conditions ordered by the Commission for each individual merger provide only short-term and ultimately inadequate protections against the RBOCs' demonstrated exclusionary and discriminatory inclinations and practices, and are simply insufficient to ensure that robust competition in the market for special access services will develop and be sustained.

Notably, the RBOC mergers of the past two years each were approved by the Commission notwithstanding record evidence that: (1) the mergers would eliminate the most significant source of actual and potential competition for special access services within each of the RBOC and affiliated ILEC operating territories;[102] (2) high barriers to entering the market for special access services would foreclose future competition;[103] and (3) RBOC consolidation in the markets for special access services would provide the

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[101] Comments of Cbeyond *et al.*, WC Docket No. 06-74, at 88-90 (filed Jun. 5, 2006); Petition to Deny of CompTel, WC Docket No. 06-74, at 11-12 (filed Jun. 5, 2006); Petition to Deny of Earthlink, Inc., WC Docket No. 06-74, at 21-27 (filed Jun. 5, 2006); Comments of Sprint Nextel Corporation, WC Docket No. 06-74, at 6-9 (filed Jun. 5, 2006); Petition to Deny of Time Warner Telecom, WC Docket No. 06-74, at 32-49 (filed Jun. 5, 2006).

[102] A report submitted by XO Communications in the Verizon/MCI and SBC/AT&T merger proceedings before the Commission shows that MCI's market share of 10% of Wholesale Metro Private Lines, over all metropolitan areas, ranked first outside of the RBOCs. Following the merger of Verizon and MCI, the market share of Wholesale Metro Private Lines owned by Verizon increased from 74% to 84%. The same study reflects that AT&T's market share of 9% of Wholesale Metro Private Lines, over all metropolitan areas, ranked second outside of the RBOCs. Following the merger of AT&T and SBC, the market share of Wholesale Metro Private Lines owned by the "new" AT&T increased from 75% to 84%. *Ex Parte* Letter from Thomas W. Cohen, Kelley Drye & Warren, LLP, Counsel for XO Communications to Marlene H. Dortch, Secretary, Federal Communications Commission, WC Docket Nos. 05-65 and 05-75 (filed Sept. 21, 2005) (enclosing Wholesale Communications Strategies, The Yankee Group, Prepared for XO Communications, January 2004); *see also supra* n.100.

[103] Comments of Cbeyond *et al.*, WC Docket No. 06-74, at 62 (filed Jun. 5, 2006); Petition to Deny of CompTel, WC Docket No. 06-74, at 11-12 (filed Jun. 5, 2006); Petition to Deny of Time Warner Telecom, WC Docket No. 06-74, at 10-16 (filed Jun. 5, 2006).

RBOCs with increased opportunities and incentives to raise special access rates farther above cost, and to engage in practices that would harm special access competition.[104] The remedies adopted by the Commission are not sufficient to redress the adverse impact of those mergers on the offering of special access services. As demonstrated by the evidence provided herein, they already have proven, to a significant degree ineffective.[105] The Commission therefore should recognize their limited value and adopt regulations that discipline special access rates in the absence of real competition, and permit competition to thrive.[106]

As an indication of the weakness of the merger condition limiting special access price increases, record evidence before the United States Court for the District of Columbia, in the Tunney Act review proceeding demonstrates that, as the result of those mergers, unreasonable price increases for special access services occurred.[107]

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104 *See supra* n. 101.

105 *See infra* n.107. The record before the United States District Court for the District of Columbia, in the Tunney Act proceeding on the mergers of Verizon and MCI, and AT&T and SBC, is replete with evidence that the RBOCs' pricing of special access services increased post-merger.

106 Another flaw with the conditions imposed by the Commission in the RBOC mergers is that they are in effect only for the short term. Specifically, those conditions will expire after thirty (30) months, in the case of Verizon, or after forty-eight (48) months, in the case of AT&T, without any further review by the Commission. Verizon/MCI Merger Order, Appendix G; AT&T/BellSouth Merger Order, Appendix F. The Commission, *sua sponte*, even reduced the duration of Special Access Condition No. 6, setting caps for the prices, terms and conditions at which AT&T may offer DS1 and DS3 channel termination services, from forty-eight (48) months to thirty-nine (39) months, after approving the merger of AT&T and BellSouth. *In the Matter of AT&T Inc. and BellSouth Corporation Application for Transfer of Control*, WC Docket No. 06-74, Order on Reconsideration, FCC 07-44, 22 FCC Rcd 6285 (rel. Mar. 26, 2007).

107 *U.S. v. SBC Communications, Inc. and AT&T Corp.*, Civil Action No. 1:05CV02102 (EGS); *U.S. v. Verizon Communications, Inc. and MCI, Inc.*, Civil Action No. 1:05CV02103 (EGS) (consolidated), ActTel's Reply Memorandum in Opposition to

Specifically, by eliminating key lower-priced providers of competing special access services (AT&T and MCI), downward pressure on the pricing of special access services by SBC and Verizon, pre-merger, was relieved,[108] and pricing that was showing signs of decline "stabilized."[109] Moreover, the acquiring companies (Verizon and the "new" AT&T), having been freed from competition, implemented direct increases to DS1 and DS3 private line services not within the jurisdiction of the Commission (*i.e.*, intrastate special access services).[110]

Importantly, the conditions imposed on mergers of Verizon and MCI, and of SBC and AT&T, also are limited in scope to the pricing levels of the merged entities and do not prohibit other practices that may undermine or otherwise defeat competition within the markets for special access services.[111] Despite several *ex parte* submissions by Qwest,[112] the Commission elected to ignore substantial evidence of anti-competitive

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the United States' Motion for Entry of Final Judgments (filed Jun. 6, 2006) ("ActTel Merger Brief") at 15-19.

108 *Id.* In the Tunney Act proceeding, ActTel submitted substantial evidence, including pre-merger statements by Verizon and SBC, demonstrating that competition within the market for special access services was declining before the mergers of 2005.

109 ActTel Merger Brief at 15-17.

110 *Id.* at 17-18, n. 21 (and associated Exhibit). In that proceeding, ActTel demonstrated that AT&T announced price increases for DS1 and DS3 Local Private Lines in seven states within one year of merging with SBC.

111 *See* SBC/AT&T Merger Order at Appendix F; Verizon/MCI Merger Order at Appendix G.

112 *See, e.g., Ex Parte* Letter from Melissa E. Newman, Vice President – Federal Regulatory, Qwest to Marlene H. Dortch, Secretary, Federal Communications Commission Re: WC Docket No. 05-65 (Oct. 5, 2005); *Ex Parte* Letter from Melissa E. Newman, Vice President – Federal Regulatory, Qwest to Marlene H. Dortch, Secretary, Federal Communications Commission Re: WC Docket No. 05-65 (Sept. 27, 2005).

practices by SBC, even prior to consummating its proposed merger with legacy AT&T.[113] For example, in re-negotiating its contract-based special access service arrangements, SBC attempted to impose on its existing customers, including Qwest, terms and conditions of service that effectively would prohibit any migration to special access services offered by SBC's competitors, or to other SBC services, including UNEs.[114] In particular, SBC's "take-it-or-leave-it" special access service offering included, for the first time: (1) stringent limitations on grooming of special access facilities, either to move from SBC's special access services to competing special access services, or other, more cost-effective SBC services; and (2) limitations on Qwest's use of UNEs, to five percent of Qwest's total local access spend with SBC.[115] Such provisions that perpetuate carriers' reliance on the ILECs' special access services through limitations on the use of UNEs are anti-competitive and discriminatory.[116]

In addition, commenters in the AT&T/BellSouth merger proceeding advised the Commission that high-volume commitments and associated penalties for early termination of service contracts, place significant limitations on the use of non-ILEC special access services, where those services are available.[117] For example, as CompTel explained, "because only the incumbent can supply *all* of any customer's special access

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113 SBC/AT&T Merger Order, Appendix G.

114 *See supra* n.86.

115 Qwest's October 5, 2005 Ex Parte Letter at 3-5.

116 The ILECs have imposed similar limitations on tariffed special access services. *See, e.g.*, Ameritech Operating Companies, FCC Tariff No. 2, Access Service, 7th Revised Page 659, Section 19 (Effective Oct. 21, 2003); Southwestern Bell Telephone Company, FCC Tariff No. 73, Access Service, 3rd Revised Page 38-1, Section 38 (Effective Oct. 17, 2003).

117 Petition to Deny of CompTel, (*AT&T and BellSouth Corp. Application for Transfer of Control*) *WC* Docket No. 06-74 at 13-16 (filed Jun. 5, 2006).

demand, the incumbent can therefore condition the availability of discounts on certain circuits (the majority, for which no competitive alternative is available) on the customer's commitment to transfer the 'competitively sensitive' portion of its demand to the incumbent."[118] Because subscribers face high termination penalties when volume commitments are not reached, those costs are far greater than any saving recouped through cheaper special access services from non-ILEC providers.[119]

Since the initial filing of comments and reply comments in this proceeding, the mergers of Verizon and MCI, SBC and AT&T, and the "new" AT&T and BellSouth, have all resulted in the national market for special access services being dominated by two RBOCs: AT&T and Verizon. The duopoly that recently has emerged brings with it the danger of collusion between the "new" AT&T and Verizon. In prior merger review proceedings, the Commission determined that the risk of collusion is greatest where the number of ILECs is reduced and high market barriers exist.[120] Importantly, the Commission also determined that mergers resulting in duopoly (or monopoly) tend to harm the public interest, and therefore warrant strong presumptions of illegality under existing antitrust doctrines.[121] At bottom, the Commission must reconsider its regulation of special access pricing in light of the dramatically changed, post-merger market conditions.

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118 *Id.*

119 *Id.*

120 *Id.* at 14 (citing SBC/Ameritech Merger Order ¶ 104).

121 *Id.* at 16 (citing *Application of EchoStar Communications Corporation, General Motors Corporation and Hughes Electronics Corporation (Transferors) and EchoStar Communications Corporation (Transferee)*, Hearing Designation Order, 17 FCC Rcd 20559 ¶ 103 (2002).

B. Decreased Availability of UNEs Leads to Increased Market Power in the Provision of Special Access

Section 251 of the 1996 Act obligates ILECs to unbundle loop and dedicated transport network elements, and to offer such network elements subject to the terms and conditions of state commission approved interconnection agreements, at cost-based rates.[122] Furthermore, Section 271 of the 1996 Act obligates the RBOCs to unbundle loop and dedicated transport network elements, and to offer such network elements at rates, and subject to terms that are just and reasonable.[123] Those high-capacity (DS1 and DS3 capacity) loop and dedicated transport network elements offered pursuant to Section 251 and, to a very limited extent, Section 271, enable CLECs to deploy economically facilities-based networks in competition with the ILECs. In contrast, special access circuits, because they are priced far above cost and contain onerous terms and conditions, are poor substitutes and inhibit facilities-based deployments.

Since the initiation of this proceeding, federal and state commission decisions impacting the ILECs' statutory unbundling obligations have resulted in growing limitations on access to Section 251 UNEs. Moreover, several state commissions, with few exceptions, have declined to enforce Section 271 unbundling obligations through the interconnection agreement arbitration process or otherwise. Those that have exercised Section 271 authority have largely been reversed by the federal courts. As a result, the rates, terms and conditions for Section 271 network elements in most states are simply those that apply to the RBOCs' month-to-month special access offerings.

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122 47 U.S.C. § 251(c)(3).

123 47 U.S.C. § 271(c)(2)(B)(ii).

1. High Capacity Loops and Dedicated Transport Facilities

Since the initial filing of comments and reply comments in this proceeding, carriers have, in large part, implemented the Commission's *TRRO* and numerous state commissions have issued decisions interpreting it. Per the *TRRO,* ILECs are no longer obligated to provide certain high-capacity (DS1 and DS3) loop and dedicated transport UNEs in wire centers or on routes that meet or exceed the non-impairment thresholds established by the Commission.[124] The initial transition period for high-capacity loop and dedicated transport UNEs deemed "non-impaired" by the ILECs on the effective date of the *TRRO* expired on March 11, 2006.[125] Those UNEs subject to the initial transition period, with rare exception, already have been converted or are slated to be converted to unreasonably priced special access services or, in rare instances, services provided over other competitive facilities.[126] Importantly, effective March 11, 2005, the ILECs also are no longer obligated to unbundle dedicated transport UNEs that do not connect ILEC wire centers (*i.e.,* entrance facilities).[127]

In combination, these new Commission rules ending access to UNEs have resulted in the loss of critical inputs by facilities-based competitors to ILECs, thereby increasing the incumbents' market power in the provision of special access services.***

V. THE COMMISSION SHOULD REVOKE PHASE II PRICING FLEXIBILITY, REINITIALIZE RATES, AND BAN THE USE OF EXCLUSIONARY OR ANTI-COMPETITIVE TERMS AND CONDITIONS

124 47 C.F.R. §§ 51.319(a)(4)(i); 51.319(a)(5)(i); 51.319(e)(2)(ii)(A); 51.319(e)(2)(iii)(A).

125 47 C.F.R. §§ 51.319(a)(4)(iii); 51.319(a)(5)(iii); 51.319(e)(2)(ii)(C); 51.319(e)(2)(iii)(C).

126 Covad *Clancy Decl.* ¶ 6; XO *Koppersmith Decl.* ¶ 9.

127 47 C.F.R. § 51.319(e)(2)(i).

The existing special access pricing flexibility regime is fatally flawed, and there is no reason to believe that recent market and regulatory developments – namely, the industry consolidation over the last few years and the elimination of UNEs in certain areas – will result in special access prices being regulated by market forces. In fact, just the opposite is the case. As demonstrated herein, pricing flexibility has resulted in special access rates that are unjust, unreasonable, discriminatory, and not in the public interest. The Joint Commenters join other competitive carriers and users of special access services in emphasizing that a substantial overhaul of the Commission's current price cap and pricing flexibility regime is necessary to constrain the ILECs' ability to exercise their market power in the special access markets.[128]

There are two principal components to the reform proposed by the Joint Commenters. First, in view of the overwhelming evidence that ILECs remain dominant in the provision of special access services and have used their market power to constrain competition and harm consumers, the Commission should reinstate an effective system of price cap regulation that ensures that special access prices are set at just and reasonable levels. Second, the Commission should act to eliminate the exclusionary pricing practices of many of the ILECs, including term and volume commitments with excessive termination penalties, forced UNE/special access conversion, and non-advocacy requirements.[129]

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128 *See, e.g.*, Ad Hoc Comments, WC Docket No. 05-25, at 16-21 (filed June 13, 2005); ATX Comments, WC Docket No. 05-25, at 5-10 (filed June 13, 2005); Ionary Comments, WC Docket No. 25-25, at 1-3 (filed June 13, 2005); PAETEC Comments, WC Docket No. 05-25, at 4-5 (filed June 13, 2005); Nextel Reply Comments, WC Docket No. 05-25, at 14-28 (filed Jul. 29, 2005).

129 Joint Commenters oppose Nextel's proposal to replace collocation triggers with *TRRO* non-impairment standards. *See* Nextel Reply Comments, WC Docket No. 05-25, at 32-34 (filed July 29, 2005). As demonstrated herein, these standards

In enacting the first component of the remedy proposed by Joint Commenters, the Commission should begin by reinitializing ILEC tariffed special access price caps at an 11.25% rate of return. The Commission should also adopt an X-factor, which would require the ILECs to reduce their rates by a certain percentage each year, thereby requiring the ILECs to share their productivity gains with their customers. More specifically, the Commission should adopt, at least on an interim basis subject to further review, a 5.3% X-factor in order to ensure that the ILECs' special access rates are established at reasonable levels.[130] Indeed, some commenters have felt that an 11.25% rate of return and a 5.3% X-factor is overly generous toward the ILECs.[131]

Additionally, once existing rate levels for special access have been reinitialized and the X-factor set, the Commission could grant downward pricing flexibility across all access markets. Downward pricing flexibility would allow the ILECs to reduce prices in response to competition and provide a self-executing regulatory device that should automatically assure the appropriate regulatory treatment of ILEC rates.[132] Since market forces would work to restrain ILECs from raising prices where sufficient competition is present, they have no legitimate need for pricing flexibility in the upward direction.

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have resulted in the elimination of UNEs despite the absence of economic competitive or self-supply options. XO *Govil Decl.* ¶ 31-34; Covad *Clancy Decl.* ¶ 10-13.

130 Nextel Reply Comments, WC Docket No. 05-25 (filed July 29, 2005).

131 *See, e.g.*, Ad Hoc Telecommunications Users Committee Comments, WC Docket No. 05-25, at 37-38 (filed July 13, 2005) ("the 11.25% return level is likely an extremely generous mark given current market conditions and can in no way be viewed as confiscatory, or even disadvantageous, for the ILECs.").

132 *See e.g., Competition in Access Markets: Reality or Illusion, A Proposal for Regulation Uncertain Markets Prepared for the Ad Hoc Telecommunications Users Committee,* August 2004 at 12 ("*ETI White Paper*"), attached to the Ex Parte Letter from Colleen Boothby, Counsel for Ad Hoc Telecommunications Users Committee, to Marlene H. Dortch, FCC, WC Docket No. 04-313 (filed Sep. 30, 2004).

With respect to the second component of the relief proposed by the Joint Commenters, the elimination of exclusionary and anti-competitive terms and conditions would do much to help ensure an open and fair marketplace for special access services. Currently, numerous ILECs tie special access pricing to very high term and volume commitments with excessive termination penalties. Such preferences can unfairly favor larger service providers over smaller service providers and, in so doing, can stifle competition. Similarly, the Commission should forbid the ILECs from entering into contracts that require a service provider to convert all or a percentage of its UNEs to special access services, to guarantee a certain percentage of "spend" on special access, or to agree only to purchase special access services in the future. Finally, the ILECs' new trend toward presenting discounted offerings to customers who agree not to oppose ILEC interests in Commission proceedings is not only anti-competitive, it is contrary to public policy. In order to reach proper results in its proceedings, the Commission must ensure that all interested parties are free to participate fully and in an unencumbered manner. Attempts to limit this right are essentially efforts to undermine the Commission and the effectiveness and legitimacy of its decision making process.

Notably, to ensure that the relief enacted in this docket is meaningful, the Commission should adopt a "fresh look" policy for all special access agreements currently in force.[133] A fresh look policy would give special access customers an opportunity to terminate current arrangements for a set period of time after the effective date of a Commission order in this proceeding. During this time, the terms of these contracts could be renegotiated to comply with the new rules governing the maximum

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133 *See, e.g., Expanded Interconnection with Local Telephone Company Facilities, Second Memorandum Opinion and Order on Reconsideration,* 8 FCC Rcd 7341 (1993).

permissible charge by the ILEC and to remove any illegal terms or conditions. In this case, a fresh look period is clearly warranted by the market distortions that have occurred since deregulation of the special access market began. The exorbitant rates charged and anti-competitive terms imposed by ILECs must be corrected as soon as possible in order to ensure that competitive telecommunications options will still be available to individual consumers as well as to small- and medium-sized businesses.

The Commission is authorized to order fresh look provisions in connection with changes to its special access pricing regulations.[134] Importantly, the Commission has recognized that the "existence of long-term access arrangements… raises potential anti-competitive concerns since they tend to 'lock up' the access market, and prevent customers from obtaining the benefits of the new, more competitive interstate access environment."[135] Therefore, the Commission has adopted fresh look provisions in the context of prior changes to its special access pricing regulations, where such provisions would serve the public interest, and would eliminate ongoing use of special access prices

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134 *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, Order, 11 FCC Rcd 15499, ¶ 1095 (1996). In the *Local Competition Order*, the Commission declared that it has "ample authority under Section 4(i) of the 1934 Act as well as Section 251 of the 1996 Act, to order this remedy," and that "[c]ourts have held that 'the Commission has the power to prescribe a change in contract rates when it finds them to be unlawful . . . and to modify other provisions of private contracts when necessary to serve the public interest." *Id.* (quoting *Western Union Tel. Co. v. FCC*, 815 F.2d 1495, 1501 (D.C. Cir. 1987)).

135 *Expanded Interconnection with Local Telephone Company Facilities*, Memorandum Opinion & Order, 7 FCC Rcd 7369, ¶ 201 (1992), *recon.* 8 FCC Rcd 7341, 7342-59 (1993) (fresh look to enable customers to take advantage of new competitive opportunities for special access under expanded interconnection), *vacated on other grounds and remanded for further proceedings sub nom. Bell Atlantic Tel. Cos. v. FCC*, 24 F.3d 1441 (1994). *See Expanded Interconnection with Local Telephone Company Facilities*, Memorandum Opinion & Order, 9 FCC Rcd 5154 (1994).

that the Commission determined to be unlawful.[136] To the extent that the Commission adopts new or modified special access pricing regulations in this proceeding, the Commission also should adopt fresh look provisions to ensure that such regulations will benefit all customers.

CONCLUSION

The Commission should expeditiously act to modify existing regulations governing ILEC special access pricing flexibility in the manner described herein.

Respectfully submitted,

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136 *See id.*